147

FILE COPY

No. [redacted] 3

IN THE

Supreme Court of the United States

OCTOBER TERM 1942

A. M. ANDERSON, RECEIVER OF NATIONAL BANK OF KENTUCKY, OF LOUISVILLE,

Petitioner,

v.

KATHERINE KIRKPATRICK ABBOTT, ADMINISTRATRIX WITH THE WILL ANNEXED, OF THE ESTATE OF DAVID J. ABBOTT, DECEASED, ET AL.,

Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT AND BRIEF FOR PETITIONER.

ROBERT S. MARX,
FRANK E. WOOD,
EDWARD M. BROWN,
HARRY KARFIS,
Attorneys for Petitioner.

Of Counsel,
NICHOLS, WOOD, MARX & GIESTER.

THE JOHNSON & HARDIN CO., LAW PRINTERS
CINCINNATI, OHIO

CONTENTS

TABLE OF CASES

STATUTES AND MISCELLANEOUS MATTER

No._____

IN THE

Supreme Court of the United States

OCTOBER TERM 1942

A. M. ANDERSON, RECEIVER OF NATIONAL BANK OF KENTUCKY, OF LOUISVILLE,

Petitioner,

v.

KATHERINE KIRKPATRICK ABBOTT, ADMINISTRATRIX WITH THE WILL ANNEXED, OF THE ESTATE OF DAVID J. ABBOTT, DECEASED, ET AL.,

Respondents.

PETITION FOR WRIT OF CERTIORARI TO THE UNITED STATES CIRCUIT COURT OF APPEALS FOR THE SIXTH CIRCUIT

To the Honorable the Chief Justice and the Associate Justices of the Supreme Court of the United States:

A. M. Anderson, Receiver of the National Bank of Kentucky, of Louisville, prays that a writ of certiorari issue to review the decree, entered May 4, 1942, and the order denying petitioner's motion for a rehearing thereof, en-

tered June 5, 1942, in the United States Circuit Court of Appeals, Sixth Circuit. The decree and order affirmed a judgment of the United States District Court for the Western District of Kentucky, which finally dismissed petitioner's Bill of Complaint. The Bill sought to recover, from the respondents, for the benefit of the unpaid depositors of the insolvent National Bank of Kentucky, their proportionate part of the statutory *individual* liability amounting to Four Million Dollars, assessed against several thousand shareholders thereof by the Comptroller of the Currency.

SUMMARY STATEMENT

National Bank of Kentucky, located at Louisville, was the largest bank in the South. Its capital was four million dollars; deposits about forty million. It failed November 16, 1930; closed by voluntary resolution of its Board of Directors. The National Bank Examiners' reports, for three full years before its failure clearly indicated its eventual collapse unless a sound house-cleaning was put into effect. (Ex. 13, 14, 15, 16, 17, pp. 224, 314, 407, 486, 572.)* Copies of these Bank Examiners' reports, two each year, were sent to the Bank as provided by law; so its failing condition was known to its officers, and should have been known by all its directors. (Ex. 31-1 to 33-25 inclusive, pp. 1275-1305.) The non-officer directors, however, disclaimed knowledge of the conditions; said they had complete confidence in James M. Brown, President; said they did not see the examiners' reports, and did not know of the Bank's failing condition.

---

* In this petition and brief exhibits are referred to by number and by page at which they appear in the five photo-offset volumes. References to the three-volume printed record are by volume number and page. Italics and other emphasis is ours unless otherwise noted.

Brown was the dominant figure. His authority was supreme and unquestioned. It is admitted that he knew the Bank's true condition. He was personally involved and seemed unable to furnish the sound financial leadership necessary to avert the inevitable failure. Instead, with full co-operation of the directors and stockholders, he resorted to grandiose financial schemes leading eventually to a large chain of banks operated through a bank-stock holding company, BancoKentucky Company.

In 1927, National Bank of Kentucky and a large State bank, Louisville Trust Company, were "unified"; substantially all the stock of both banks being transferred to trustees who issued Trustees Participation Certificates therefor. (Ex. 7, p. 115; Ex. 10, p. 152.) Thereafter these two banks were operated through identical Boards of Directors. (Ex. 77, p. 1753.) Extensive publicity attended this "unification" but publicity alone would not cure the financial ills of National Bank of Kentucky. The National Bank Examiners' criticisms continued and became more insistent. Large charge-offs were suggested. Deposits were shrinking. Serious difficulty was experienced in maintaining legal reserve requirements. Brown evolved one scheme after another to escape the crash. He tried to denationalize the Bank by consolidating it with Louisville Trust Company as a State Bank; thus to escape national supervision. (R. III, p. 20.) This failed because of four million dollars in "substandard" assets. (Ex. 54, pp. 1479, 1481.)

Finally, in June, 1929, while the Bank Examiners were in the bank making an examination Brown proposed the organization of a big bank stock holding company, Banco-Kentucky Company, with "twenty million" dollars capital; and upon the promise that the holding company would be promptly organized and would "acquire" and "work out" the Bank's criticized assets the "matter of charge-off was dropped" by the National Bank Examiners. (Ex. 17, p. 612.)

BancoKentucky Company, conceived to bolster up a failing National Bank, was incorporated on July 19, 1929, under the laws of Delaware. (R. II, p. 81.) It was authorized to issue two million shares at ten dollars each. Its prospectus, signed by the two banks and their identical Boards of Directors, was sent to each shareholder of the "unified" National Bank of Kentucky and Louisville Trust Company. It stated that (Ex. 24-3, p. 1140.)

> "the two banks, and the business conducted by them, should be reorganized by adding to this group a third corporation, which will make the operation of these banking institutions more profitable, expand their facilities, and thus develop for the entire group new and profitable financial opportunities and connections."

And provided that:

> "It is an essential part of this reorganization that the shares of this corporation (or at least a substantial majority thereof) be owned by the Trustees Participation Shareholders, *and that it be managed and operated by the Boards of Directors and the officers of the two banks.*

It was also a prerequisite part of the plan that Banco hold at least a majority of the Bank stock.

This prospectus offered the "entire capital stock" of BancoKentucky to the shareholders of the two banks; two shares for each Trustees' Participation Certificate and the remainder at twenty-five dollars per share. Substantially all the certificate holders made the exchange. (R. II, pp. 93, 97.) The plan was so arranged that no tax liability would be imposed on the exchange. The creation of the holding company was described as a "reorganization" (Ex. 24-3, p. 1140). It was "at once seen that the taxable gain would be very large" (Ex. 25, p. 1145) unless this

was so, and the organizers took every step so that the exchange of bank stock for holding company stock would be "made to appear (so far as the bank stockholders are concerned) as a mere receipt of the same property in another form, and not as a closed transaction wherein they part with one species of property in exchange for an entirely different species of property." (Ex. 25-5, p. 1157.) The Court of Appeals held that an out and out exchange of assessable stock for non-assessable stock was made but the trading of bank stock for holding company stock simply cannot be a "reorganization" to escape taxes, and a sale, to escape assessment.

A great many certificate holders in addition to making the exchange, and in response to a regular promotion campaign put on by the banks and aided by loans made by the National Bank of Kentucky amounting to more than Five Million Dollars on the security of BancoKentucky stock, subscribed for additional shares. (Ex. 134-5, p. 1934.) Some subscriptions were accepted from non-certificate holders. Nearly ten million dollars in cash thus came into the treasury of BancoKentucky Company. Instead of utilizing this new money to clean up the National Bank of Kentucky, as promised to the Bank Examiners, it was paid out almost immediately to purchase the controlling stock in a number of other banks, some of which was paid for in cash and some in BancoKentucky stock. (R. II, pp. 1195-97.) Banco promoters represented to the stock exchange "it is the intention of the management to employ its cash for acquiring additional banks." (Ex. 74, p. 1723.)

The following pertinent facts about BancoKentucky Company appear in the record. It was incorporated in Delaware July 19, 1929. Its President and Secretary-Treasurer were President and Cashier respectively of National Bank of Kentucky. (Ex. 23, pp. 1063, 1099.) Its directorate and the unified banks' directorate were identi-

cal. (Ex. 23, pp. 1055, 1056.) It had no employees; paid no salaries or wages; had no office, office furniture or equipment. It did not even have a telephone. (R. II, pp. 102, 122, 280.) It had only three small record books: cash journal, ledger, and security record (Ex. 65, 65A, 65B, pp. 1496, 1575, 1621A), and these were all kept by and in the desk of the Cashier of the bank. (R. II, p. 282.) It did not have a correspondence file. It never even qualified to do business in Kentucky. Ky. Stat. Sec. 571. (R. II, pp. 102, 103.) It is significant that notwithstanding his annual oath to the contrary, as required by law (12 U. S. C. 73), not a single director of National Bank of Kentucky was a "good faith" owner of a single share of its stock.*

Banco began its actual business existence in October, 1929. It failed ingloriously in November, 1930, with no substantial assets except bank stocks; and most of these banks became insolvent at the same time. (Ex. 23, p. 1120; Ex. 179, p. 2099.) During the short period that it was in existence it acquired the following bank stocks through exchange of its stock and for cash:

Number of Bank Shares Held by Banco			Name of Bank	Percentage of Stock Held by Banco
38,000	out of	40,000	National Bank of Kentucky, Louisville	95%
16,625	"	17,500	Louisville Trust Co.	95%
47,854	"	60,000	Pearl Market Bank & Trust Co., Cinti., O.	80%
44,290	"	50,000	Brighton Bk. & Trust Co.	89%
548	"	600	Central Sav. Bk., Cov., Ky.	91%+
2,099	"	6,500	Peoples Liberty Bk. & Tr. Co., Covington, Ky.	32%+
6,925	"	7,500	First National Bank, Paducah, Ky.	92%+
7,125	"	8,000	Ashland National Bk., Ashland, Ky.	89%+
2,713	"	3,000	Security Bank, Louisville, Ky.	90%+
575	"	1,000	Mechanic's Tr. & Sav. Bk., Paducah, Ky.	58%—

The above bank stocks together with "an infinitesimal amount" (R. III, p. 167) of Insurance Stock and a concealed unauthorized note of the President Brown (infra, p. 7) were the entire portfolio of Banco.

* (R. II, p. 247; Exhibits 23, 92-95, 81-85, 90-2, 90-5, 90-7 to 90-12, 91, 94, pp. 1099, 1822-25, 1797-1801, 1809, 1812, 1814-1819, 1820, 1824.)

BancoKentucky Company, as its name significantly indicates, was a bank-stock holding company pure and simple. It was so listed on all the stock exchanges. (Ex. 98, p. 1829; Ex. 74, pp. 1717, 1723; Ex. 73, p. 1713; Ex. 71, p. 1695.) All the newspapers carried its market quotations under the heading of Bank stocks. (Ex. 26, pp. 1181, 1183, 1189.) The prospectus announced that Banco was organized after study of "the rapidly changing conditions in the banking business" and "in line with the trend of business and finance in this country" (Ex. 24-3, p. 1140). The "trend" was to organize holding companies. See "Hearings on Branch, Chain and Group Banking" under H. R. 141, 71st Cong., 2nd Sess. "At the end of June 1929 . . . there were in existence . . . 230 group systems in the United States which embraced about two thousand banks." (Vol. 1, Part 1, p. 43, Record of Hearings.)

During its whole existence it engaged in no business outside of acquiring and holding bank stocks except for these three simple transactions: It invested $25,000.00, less than 1/10 of 1% of its total assets (Ex. 76, p. 1739), in Union Central Life Insurance Company stock. It made an unauthorized personal loan to its President Brown. (R. II, p. 98.) The loan was concealed from the Directors of the Company. (R. II, pp. 63, 64.) At the last minute in a futile effort to save the bank it purchased some of the bank's worthless investments. (R. II, p. 97.) This last transaction, involving only one and a half per cent of its total assets, was never brought before the directors, and was rescinded by the courts after the collapse. *BancoKentucky Company's Receiver* v. *National Bank of Kentucky's Receiver*, 281 Ky. 784, 137 S. W. (2d) 357. A belated scheme to go into partnership with the insolvent Caldwell & Co., which controlled a chain of 66 banks (see table compiled from Federal Reserve Board data by Cartinhour—Branch Group and Chain Banking, p. 66; see also Ex. 103, p. 1840; Ex. 26, pp. 1207, 1212; R. II, pp. 105, 302), was never consummated. (R. I, p. 262.) It was an effort to avert failure; trying to make a good financial omelet out of two bad eggs.

National Bank of Kentucky paid dividends of $160,000.00 each quarter, equal to $16.00 per share per year on its capital stock, to BancoKentucky which distributed the exact amount to its shareholders on the very same day it was received from the bank. (R. II, p. 101.) From its organization until its failure, little more than a year, BancoKentucky's only income, except a small interest earning on deposit balances, was from dividends on bank stock. (R. II, p. 122.) During its existence it collected $1,180,858.50 dividends from its bank stocks and paid $1,253,513.00 to its stockholders. The money to pay the deficit was met by overdraft on the National Bank of Kentucky. (R. II, p. 122.)

National Bank of Kentucky failed November 17, 1930. One week later a petition for receiver was filed for Banco-Kentucky Company. (Ex. 66, p. 1676.) On February 20, 1931, the Comptroller of the Currency under Sections 64, 191, and 192 U. S. Code Title 12, then in effect made an assessment upon the shareholders of the National Bank of Kentucky of four million dollars, and directed the Receiver to collect the same. (R. II, p. 76; Ex. 5, p. 6.) Shortly thereafter the Receiver notified the stockholders of Banco-Kentucky Company of his intention to proceed against them for the collection of said assessment to the extent that he was unable to collect the same from the Receiver of the BancoKentucky Company. (R. I, p. 70; R. II, p. 76.) The Receiver of the National Bank of Kentucky was able to collect only a small part of said assessment from the Receiver of BancoKentucky Company because of its hopeless insolvency. (R. I, p. 71; R. II, p. 106.) It had no assets except bank stocks and these had become liabilities by the collapse. He therefore brought this suit against the stockholders residing in the Western District of Kentucky to recover from each their proportionate part of said assessment ($2.305 on a share of Banco, Ex. 120, p. 1871; R. II, p. 124). The depositors of the bank have received dividends to date of 77%. The assessment involved in this and kindred cases pending in other districts (D. C. Ala.; E. D. Kentucky; D. C. Mass.; E. D. Mich.; D. C. New

York; S. D. Ohio; E. D. Pa.; M. D. Tenn.; S. D. Ind.; N. D. Ill.; D. C. Va.; D. C. W. Va.) would, if collected, provide a ten per cent additional dividend.

OPINIONS BELOW

The District Court for the Western District of Kentucky filed two opinions. An opinion overruling defendants' motion to dismiss was filed April 15, 1936, and is reported in 23 F. Supp. 265. (R. I, p. 144.) The opinion on the merits dismissing the Bill of Complaint was filed March 23, 1940, and is reported in 32 F. Supp. 328. (R. I, p. 288.) Similar suits were filed and are now pending against shareholders residing in other States. A motion to dismiss the Bill of Complaint filed in the Northern District of Illinois was denied by the District Court of that State in an opinion filed February 14, 1938. *Anderson* v. *Atkinson*, 22 F. Supp. 853.

On May 4, 1942, the Circuit Court of Appeals, Sixth Circuit, affirmed the judgment of the District Court for the Western District of Kentucky. This opinion is reported at 127 F. (2d) 696. (R. III, p. 312.) The petitioner's application for rehearing (R. III, p. 327) was denied on June 5, 1942, without written opinion. (R. III, p. 355.)

JURISDICTION

Jurisdiction is conferred on this Court to review this cause by writ of certiorari by Section 240a of the Judicial Code as amended by the Act of February 13, 1925. (United States Code, Title 28, Section 347.) On August 26, 1942, an order was entered in this Court extending the time for the filing of this petition for writ of certiorari until November 1, 1942. (R. III, p. 357.)

THE QUESTION PRESENTED

The legal question presented here is: Are the owners of an insolvent national bank relieved from individual liability or "double assessment," under the then existing Federal statute because, shortly before the bank's failure, they organized a holding company and exchanged their bank shares for holding company shares?

Contrary to a long list of Federal and State Supreme Court decisions, none contra, the Circuit Court of Appeals, Sixth Circuit, affirming the District Court, held that the owners were not liable notwithstanding the fact that after the exchange the same shareholders using the holding company as an instrumentality

(1) continued in the management, operation, and control of the bank through the same officers and an identical Board of Directors, and

(2) continued to receive the dividends declared by the bank in exactly the same amount and on the very same day.

This Court has never passed directly on the question presented by this petition. It did, however, deny certiorari in the Detroit Bank-Stock Holding Company cases, *where the holding company shareholders were held liable,* on a factual situation strikingly parallel if not exactly identical to this case. *Barbour* v. *Thomas,* 86 F. (2d) 510, cert. den. 300 U. S. 670 (1937); *Ullrich* v. *Thomas,* 86 F. (2d) 678 (1936), cert. den., 301 U. S. 692 (1937).

The underlying problems presented by this case are not confined to banking or to stock assessment. The case squarely presents the question whether the holding company can be used to limit or circumvent the protection afforded to the general public by statutes enacted by Congress.

REASONS RELIED ON FOR ALLOWANCE OF WRIT OF CERTIORARI

The specific matter presents an important question of Federal law which has not been heretofore directly determined by this Court, and should now be determined.

The matters and issues involved are of general public interest and come within the class of cases indicated by the Rules to be appropriate for review.

It is also submitted that the case presents matters of substantial public interest to the community of Louisville, in that it vitally affects the welfare of thousands of depositors of National Bank of Kentucky to the extent of

potential dividends in the amount of nearly Four Million Dollars. While it is recognized that the amount involved does not of itself constitute a valid ground for review it is submitted that the interest of thousands of depositors in the outcome presents more the aspects of public welfare than private or individual controversy.

Cases involving numerous defendant stockholders are pending in district courts in the 1st, 2nd, 3rd, 4th and 7th Circuits. The present decision is not binding on any of those courts. In order that an authoritative decision may be rendered which will control all of the pending cases and thereby avoid the possibility of conflict, this case should be reviewed.

The decision of the Circuit Court of Appeals, holding that the owners of a failing national bank can organize a holding corporation such as BancoKentucky, acquire virtually all the capital stock by exchange of its stock for bank stock, continue to control the bank and get all its profits and dividends and, at the same time, shake off a statutory double liability, is in conflict with the decisions of this Court holding that corporate identity must be disregarded when the corporation becomes an instrument to circumvent and avoid the effect of a statute. *Northern Securities Co.* v. *United States*, 193 U. S. 197; *United States* v. *Lehigh Valley Railway Co.*, 220 U. S. 257; *United States* v. *Delaware L. & W. Railway Co.*, 238 U. S. 516; *C. M. & St. P. Railway Co.* v. *Minneapolis Civic & Commerce Association*, 247 U. S. 490. The Trustees Participation Certificates were held under an agreement incorporated therein that "each owner shall be subject to the same liability thereon as he would have been subject to in case he had been the owner of record" of his proportion of bank stock. (Ex. 7, pp. 8, 28, 29.) Having avoided tax liability on the exchange of Trust Certificate for holding company certificate, supra, p. 4, because the same property was retained and having contracted to pay the assessment in addition to assuming statutory liability, it would appear evident that the transformation of the form of

their certificates should not have relieved the defendants from liability.

The importance of the case is not lessened by the fact that the individual or double liability statute has since been limited, 12 U. S. C. 64a. Such a liability still remains on Federal Farm Loan Banks, 12 U. S. C. 872. The Circuit Court of Appeals (2d Circuit) has held that shareholders of such banks do not "evade their statutory stockholders' liability by organizing a corporation and transferring their shares for the holding company's shares." *Brusselback* v. *Cago Corp.*, 85 F. (2d) 20, cert. den. 299 U. S. 586. The decision of the Circuit Court of Appeals in the instant case would, on principle, permit the bank to make loans upon the sole security of the holding company stock, in violation of the statute forbidding the bank to loan upon the security of its own shares, 12 U. S. C. 83. It would permit a bank stock holding company to carry on branch and chain banking in violation of the entire spirit of the National Bank Act, 12 U. S. C. 36. It would permit interlocking directorates in violation of 15 U. S. C. 19. It would permit the shareholders to use the bank funds through the holding company to engage in many business enterprises which banks are forbidden to do. It would create additional problems of the examination and regulation of the subsidiary and parent corporation—a problem already presented to the lower courts in a controversy between a bank holding company and the Securities and Exchange Commission. *Bank of America Nat'l Trust & Savings Association* v. *Douglas et al.*, 105 F. (2d) 100 (C. C. A.—Dist. Col.). The problem of the bank holding company and its effect on stock assessment is recognized as a vital one by text writers on the subject. *Cartinhour—Branch Group and Chain Banking*, p. 245; *Bonbright and Means —The Holding Company*, pp. 319, 330.

The decision of the Circuit Court of Appeals is in direct conflict with a long line of federal and state court decisions which have uniformly ruled that the real owners of a national bank, that is, those who run the bank and get the dividends and profits, are liable for an assessment whether the stock stands in their names or not; and that such real owners cannot escape this liability by interposing a holding corporation as a shield to protect them from such liability. *Corker* v. *Soper*, 53 F. (2d) 190, cert. den., 285 U. S. 540 (1931); *Metropolitan Holding Co.* v. *Snyder*, 79 F. (2d) 263 (1935); *Harris Investment Company* v. *Hood*, 123 Fla. 598, 167 So. 25 (1936); *Fors* v. *Farrell*, 271 Mich. 358, 260 N. W. 886 (1935); *Nettles* v. *Rhett*, 94 F. (2d) 42 (C. C. A. 4, 1938); *Nettles* v. *Sottile*, 184 S. C. 1, 191 S. E. 796 (1937); *Hansen* v. *Agnew*, 195 Wash. 354, 80 P. (2d) 845 (1938); *Brusselback* v. *Cago Corporation*, 85 F. (2d) 20, cert. den., 299 U. S. 586; *Durrance* v. *Collier*, 81 F. (2d) 4 (C. C. A. 5, 1936); *White* v. *Aaronson*, 169 Misc. 593, 7 N. Y. S. (2d) 901 (1938); *Bacon* v. *Barber*, 110 Vt. 280, 6 A. (2d) 9 (1939); *Barbour* v. *Thomas*, 86 F. (2d) 510, cert. den., 300 U. S. 670 (1936); *Ullrich* v. *Thomas*, 86 F. (2d) 678, cert. den., 301 U. S. 692 (1936); *Anderson* v. *Atkinson*, 22 F. Supp. 853 (District Court Illinois, 1938); *Pearson* v. *All Borg*, 23 F. Supp. 837; *MacPherson* v. *Schram*, 112 F. (2d) 674 (C. C. A. 5, 1940); *Lucking* v. *Schram* (C. C. A. 6, 1941), 117 F. (2d) 160; *Union Guardian Trust Company* v. *Schram* (C. C. A. 6, 1941), 123 F. (2d) 579; *Flanagan* v. *Madison Square State Bank*, 302 Ill. App. 468, 24 N. E. (2d) 202 (1939); *Schram* v. *Cotton*, 281 N. Y. 499, 24 N. E. (2d) 305; *Schram* v. *Keane*, 279 N. Y. 227, 18 N. E. (2d) 136 (1938); *Partridge* v. *Ainley*, 28 F. Supp. 472 (District Court, New York, 1939); *Davis* v. *Schram* (C. C. A. 6, 1940), 111 F. (2d) 144; *Wolf* v. *Schram* (C. C. A. 6, 1940), 111 F. (2d) 146; *Gillespie* v. *Schram* (C. C. A. 6, 1939), 108 F. (2d) 39; *Galinski* v. *Adler*, 302 Ill. App. 474, 24 N. E. (2d) 205 (1939).

The leading case, holding that the stockholders of a bank stock holding company are liable for an assessment on the bank, arose out of the Detroit bank failures, where two great bank stock holding companies, Detroit Bankers Company and Guardian Detroit Union Group, Inc., dominated nearly all the banks in Michigan. The stockholders of these two great holding companies were held liable for the assessments ($35,000,000) levied on the banks by the United States District Court, 7 F. Supp. 271, by the United States Circuit Court of Appeals, 86 F. (2d) 510, 86 F. (2d) 678, and in which cases this Court twice denied certiorari, 300 U. S. 670, 301 U. S. 692. The decision in this case has been cited frequently with approval. *Adams* v. *Nagle*, 303 U. S. 532 (1938); *Munro* v. *Post*, 102 F. (2d) 686 (C. C. A. 2, 1939); *Erickson* v. *Richardson*, 86 F. (2d) 963 (C. C. A. 9, 1936); *Ericson* v. *Slomer*, 94 F. (2d) 437 (C. C. A. 7, 1938); *Schram* v. *Poole*, 97 F. (2d) 566 (C. C. A. 9, 1938); *Schram* v. *Cotton*, 281 N. Y. 499, 24 N. E. (2d) 305 (1939); *Smith* v. *Witherow*, 102 F. (2d) 638 (C. C. A. 3, 1939); *Geber* v. *Gossweyler*, 18 F. Supp. 925 (D. C. N. Y., 1937); *Powell* v. *Malone*, 22 F. Supp. 300 (D. C. N. Car., 1938); *Staudenmaier* v. *Johnson*, 30 F. Supp. 341 (D. C. Wis., 1939). See also: *Church* v. *Hubbard*, 91 F. (2d) 406 (C. C. A. 6, 1936); *Moss* v. *Furlong*, 93 F. (2d) 182 (C. C. A. 6, 1937); *Comm. of Internal Revenue* v. *Carey-Reed Co.*, 101 F. (2d) 602 (C. C. A. 6, 1939). It has been favorably commented on in numerous law review articles. The opinion is reprinted in Dodd and Baker's "Cases On Business Organization," used as a textbook at Harvard Law School.

The importance of this case is not affected by the fact that the Receiver of the National Bank of Kentucky also undertook to collect the assessment from Banco-Kentucky Company. BancoKentucky was the record owner of the bank stock. It is sought in this case to establish that the stockholders of Banco were in fact the real and beneficial owners. The Receiver's suit against Banco was for

the benefit of Banco's stockholders and the amount recovered by the Receiver was credited to them. (R. I, p. 178.) *Nettles* v. *Rhett*, 94 F. (2d) 42; *Continental Nat. Bank and Trust Co.* v. *O'Neil*, 82 F. (2d) 650; *Ericson* v. *Slomer*, 94 F. (2d) 437.

The liability of the Banco stockholders is not affected by the fact that they wrote into their Articles of Incorporation a section exempting their personal property from liability, and wrote on their certificates of stock that it was "fully paid and non-assessable." The real and beneficial owner cannot evade the liability in this manner.

This court will note the extent to which the same question presented here was before this Court in the suit brought by the Receiver of the National Bank of Kentucky against the Directors of that bank for losses due to their alleged negligence and statutory violations of duty. One of the claims of the Receiver in that case was that the directors had violated Section 83 of Title 12 of the United States Code, which provides that no national bank may make loans upon the security of its own capital stock. The loans in question were loans upon the security of BancoKentucky stock. The District Court held that loans made by the National Bank of Kentucky upon the security of BancoKentucky stock "was, in truth and in fact, making loans on the security of the shares of its own capital stock in violation of this statute." *Anderson* v. *Akers*, 7 F. Supp. 924, 951. The Court said:

> "The Directors of the National Bank of Kentucky caused to be organized this holding company, to which was given the suggestive name of BancoKentucky Company, which was, indeed, intended to be, and was, in many important respects and in a very real sense, as the record abundantly shows, the National Bank of Kentucky." *Anderson* v. *Akers*, 7 F. Supp. 924, 950.

The District Court opinion referred to above was reversed by the Circuit Court of Appeals, *Atherton* v. *Anderson*, 86 F. (2d) 518. *This Court granted certiorari,*

300 U. S. 652, and upon a partial hearing and without a full review, remanded the case for reconsideration by the Circuit Court of Appeals as to the question of common law negligence, a point not decided below, 302 U. S. 643 (1937). The Circuit Court of Appeals, upon rehearing, decided against the directors on the question of negligence, awarded the Receiver a *very large judgment*, but adhered to its former opinion with relation to the loans made on the security of BancoKentucky stock, 99 F. (2d) 883. The case was then settled and the question of the directors' liability, arising from loans made upon the security of BancoKentucky stock and arising out of the relationship and identity of the bank and holding company stock, thus escaped decision by this Court. However, the decision of the Circuit Court of Appeals in the Directors' Suit, which through settlement was not reviewed by this Court, is cited by the Circuit Court of Appeals as the principal authority for the decision in this case.

Since all the facts pertinent to the determination of this case by the Circuit Court of Appeals were undisputed written records, or were the subject of findings, the determination of this case presents only the question of law.

For all the foregoing reasons, it is respectfully submitted that this petition should be granted.

ROBERT S. MARX,
FRANK E. WOOD,
EDWARD M. BROWN,
HARRY KASFIR,
Attorneys for Petitioner.

Of Counsel,
NICHOLS, WOOD, MARX & GINTER.

BRIEF IN SUPPORT OF PETITION FOR WRIT OF CERTIORARI

OPINIONS BELOW

Opinions below have been referred to in the petition for writ of certiorari under this same caption.

JURISDICTION

The statement as to jurisdiction has been set forth in the petition.

STATEMENT OF THE CASE

The facts have been stated in the petition.

SPECIFICATIONS OF ERROR

1. The Circuit Court of Appeals erred in affirming the decision of the District Court.

2. The Circuit Court of Appeals erred in holding that the respondents could shield themselves behind the corporate entity of BancoKentucky and avoid stock assessment in this matter.

ARGUMENT

The idea of a bank-stock holding company originated, or at least assumed serious proportions, in the high finance days of 1911. It was then proposed in New York to form a giant bank-stock holding company to buy up, through exchange of holding company shares for bank shares, a great many banks, national and state, throughout the nation. Had the effort received governmental sanction, and succeeded, a few great holding companies might soon have controlled all the banks in the United States. The President saw the danger and called upon the Solicitor General for an opinion on the matter. In the opinion, Solicitor General Lehmann said:

"If many enterprises and many banks are brought and bound together in the nexus of a great holding corporation, the failure of one may involve all in a common disaster."

And he concluded that a holding company

"in its holdings of National Bank stock is in usurpation of Federal authority and in violation of the Federal law." Congressional Record, May 10, 1932, page 102-12.

What the Solicitor General prophesied came true at Louisville with its BancoKentucky; in Michigan with its Detroit Bankers Company and its Guardian Detroit Union Group, Inc. Fortunately for the nation, it did not happen in the northwest with its Northwest Bank Corporation, or in the far west with its giant Bank America Corporation.

Banco, just like Detroit Bankers and Guardian Detroit Group, was a promotion by the owners of the bank. It was promoted, not to let them go out of the banking business, but to continue and enlarge their investment therein, and increase their opportunity to profit thereby. They "distinctly provided" in the articles of incorporation of Banco and on its certificates of stock that it was "fully paid and non-assessable." What did they intend by this except to escape the assessment liability? The answer to the question will be found in the letter of Bean, President of the Trust Company, to Brown, President of the bank, written July 26, 1929 (Ex. 27, p. 1262), which states:

"Does the 'double liability' apply to BancoKentucky Company stock as it does to stock in the banks? NO; one of the advantages of transferring your bank stock for BancoKentucky Company stock is that you are relieved of the double liability clause which applies under the Kentucky law."

This court has consistently held that:

> ". . . they (owners of national bank stock) cannot enjoy the benefits accruing to shareholders and escape liability for the contracts, debts and engagements of the bank." (Parenthetical addition ours.) *Christopher* v. *Norvell*, 201 U. S. 216, 229.

The decisions from the earliest cases involving stock assessment liability adhere to and extend the principle that technicalities and subterfuges will be disregarded to discover the real, true and beneficial owners of the shares of the insolvent bank in order that such owners may be held liable to assessment.

> "As to such owners (real owners) the law looks through subterfuges and apparent ownership and fastens the liability upon the shareholders to whom the shares really belong." (Parenthetical addition ours.) *Ohio Valley National Bank* v. *Hulitt, Receiver*, 204 U. S. 162, 168.

The transferor has been held to be liable as actual owner where transfer of stock was made to a financially irresponsible person for the purpose of evading assessment and where the transferor continued to be the true owner. *National Bank* v. *Case*, 99 U. S. 628 (1878). The same rule was followed in *Bowden* v. *Johnson*, 107 U. S. 251 (1882), amplified in *Stuart* v. *Hayden*, 169 U. S. 1 (1897); *McDonald* v. *Dewey*, 202 U. S. 510 (1906); *Pauly* v. *State Loan*, 165 U. S. 606 (1897); *Ohio Valley National Bank* v. *Hulitt*, 204 U. S. 162 (1907).

Where the stock was transferred to a minor child who could not respond to assessment, this Court has held the transferor liable. *Early* v. *Richardson*, 280 U. S. 496 (1930).

In cases where the stock was transferred to a trustee for the purpose of taking advantage of the statute which provides that the trustee shall only be liable to the extent of

trust assets in his possession, 12 U. S. C. 66, it was held that the beneficial and real owner would be liable. *English* v. *Gamble*, 26 F. (2d) 28 (C. C. A. 8, 1928); *O'Keefe* v. *Pearson*, 73 F. (2d) 673 (C. C. A. 1, 1934); *Schlener* v. *Davis*, 75 F. (2d) 371 (C. C. A. 5, 1935).

A state court decision which sums up the law is *Fors* v. *Farrell*, 271 Mich. 358, 260 N. W. 886 (1935):

> "That neither an individual nor a corporation can, through a trust arrangement, or by other indirect means or circumlocution, possess as an owner and enjoy the beneficial interest in bank stock without assuming the contingent liability of a stockholder's assessment imposed by law. To hold otherwise would be to nullify the protection given the bank creditors by the statute imposing double liability." (P. 891.)

In more recent cases involving the use of a holding corporation as a bulwark against stock assessment, the courts have constantly held that the shareholders of the holding company are liable for assessment. *Corker* v. *Soper*, 53 F. (2d) 190 (C. C. A. 5, 1931); *Metropolitan Holding Co.* v. *Snyder*, 79 F. (2d) 263 (C. C. A. 8, 1935). The corporate fiction of the holding company was disregarded. *Durrance* v. *Collier*, 81 F. (2d) 4 (C. C. A. 5, 1936); *Fors* v. *Farrell*, supra; *Harris Investment Co.* v. *Hood*, 123 Fla. 598, 167 So. 25 (1936); *Nettles* v. *Sottile*, 184 S. C. 1, 191 S. E. 796 (1937); *Brusselback* v. *Cago Corp.*, 85 F. (2d) 20 (Cert. denied, 299 U. S. 586); *Nettles* v. *Rhett*, 94 F. (2d) 42; *Hansen* v. *Agnew*, 195 Wash. 354, 80 P. (2d) 845.

The Supreme Court of Michigan has said:

> "In a proceeding to enforce stockholders' liability, it is of little or no importance as to how many paper ownerships or holdings in trust may intervene between the bank that issued the stock and the ultimate

or actual owner thereof. The beneficial owner is liable for stock assessment. . . . Surely it was never intended that this wholesome statutory provision (for double assessment) should be nullified by resort to indirect corporate holdings of such stock."

". . . its corporate structure cannot be used as a shield behind which an actual and beneficial owner of such stock may escape the statutory liability to insolvent bank's creditors." *Fors* v. *Farrell, supra.* (Pp. 889, 890.)

The Sixth Circuit Court of Appeals has held shareholders of a holding company liable for an assessment levied on one of the subsidiary banks and in that case this Court has denied certiorari. *Barbour* v. *Thomas*, 86 F. (2d) 510 (Cert. denied, 300 U. S. 670); *Ullrich* v. *Thomas*, 86 F. (2d) 678 (Cert. denied, 301 U. S. 692). The corporate entity will be disregarded when necessary to avoid a fraud or to prevent an evasion of a statute. Wormser, "The Disregard of Corporate Fiction," pp. 36, 44, 51, 59.

This rule has been followed by this Court when to give sanctity to the corporate entity would result in circumventing a statute enacted for the protection afforded to the public by statute. *Northern Securities Co.* v. *United States*, 193 U. S. 197; *United States* v. *Lehigh Valley Railway Co.*, 220 U. S. 257; *United States* v. *Delaware L. & W. Railway Co.*, 238 U. S. 516.

In *C. M. & St. P. Ry. Co.* v. *Minneapolis Civic and Commerce Association*, 247 U. S. 490 (at 501), this Court said:

". . . the courts will not permit themselves to be blinded or deceived by mere forms of law, but, regardless of fictions, will deal with the substance of the transaction involved as if the corporate agency did not exist and as the justice of the case may require."

COURT OF APPEALS OPINION

The opinion of the Court of Appeals is analyzed in detail in the "Petition for Rehearing" found in the Record, Volume 3, page 327.

The Court of Appeals correctly concluded that the trust certificates, for which the bank stock was exchanged in the so-called "unification" of National Bank of Kentucky and Louisville Trust Company in 1927, was "the equivalent of bank stock" and that the holders thereof were "the real, beneficial shareholders of the National Bank of Kentucky." It based this conclusion upon the fact that the owners of the bank stock "carefully provided" that they should continue to be liable for any assessment. The Court then concludes that since they made no such careful provision for liability when they exchanged for Banco-Kentucky stock, they had, therefore, successfully evaded the statutory liability, and particularly so because they wrote a non-assessment section in the Articles of Incorporation and carried it on the stock certificates. It is submitted that a bank stockholder cannot so easily excuse himself from liability. The only transfer of bank stock which releases the shareholder from this statutory liability is an "out and out" transfer, whereby the shareholder completely severs himself from his stock interest in the bank and completely divests himself of his opportunity of having a voice in its control, or the receipt of any of its earnings. This Court long ago said in *National Bank* v. *Case*, 99 U. S. 628 (632, 633):

> "It is not every transfer that releases a stockholder from his responsibility as such. . . . (Liability continues if) the 'privileges and possible benefits of ownership continue.'" (Parenthetical insertion ours.)

Notwithstanding the fact that the bank examiners' reports for three full years had indicated that the bank was in financial straits, the appellate court said that "no probability of assessment" appeared when bank shares were exchanged for Banco shares. Liability does not depend upon pending insolvency. It arises by virtue of statute and depends upon ownership. The owner is the one who enjoys the "privileges and possible benefits" of the bank. *National Bank* v. *Case*, supra. What privilege or benefit did the owners of National Bank of Kentucky give up when they exchanged for Banco shares? In the words of their own lawyer, they kept "the same property in another form." Louisville Trust Company said it "was in its essence a mere continuation and retention of the ownership of Trustees Participation shares," which were conceded to be the equivalent of bank stock. Exhibit 122, pages 1886, 1887, 1890. See also Exhibit 123, p. 1896.

The Court of Appeals concluded that BancoKentucky was not organized for the primary purpose of escaping double liability. It is not necessary to quarrel with this conclusion. BancoKentucky was promoted by the owners of the bank to enable them to continue in the banking business, not for the purpose of getting out of the banking business. As an incident, they provided as best they could that the Banco shares should not be assessable and by the language of their charter and the words on their stock certificates, as evidenced by Bean's letter to Brown, *infra*, page 18, they knew very well that they were attempting to escape this liability.

The Court of Appeals, in its opinion, makes a great deal out of the fact that three million dollars of the cash raised by Banco was not invested in bank stocks. This statement is completely answered by the fact that five million dollars

of Banco's cash assets came out of the National Bank of Kentucky upon loans made solely upon the security of Banco stock and that over two million of said amount was lost by the National Bank of Kentucky. And in any event, the three million dollars was not "invested" by Banco. Twenty-five thousand dollars was invested in Union Central Life Insurance Company stock. Brown took two million dollars of the invested three million dollars without asking anybody about it, substituted his note therefor and no one knew that Banco had Brown's note until after the failure. The remainder of the "invested" three million dollars went to lift worthless assets out of the National Bank of Kentucky on the eve of its failure. This transaction was rescinded by the courts. The Caldwell deal was never consummated. Therefore, it is undisputed in the record that all of BancoKentucky's cash was invested in bank stocks except the twenty-five thousand dollars in Union Central shares.

CONCLUSION

In conclusion, therefore, it is submitted that the Record undisputably shows that BancoKentucky Company was organized to support a failing national bank; organized by its owners in order that they might continue in the banking business on a grander scale; and organized for the purpose of holding double liability bank stocks. Its doing business in Kentucky was unlawful because it never qualified to do business there. (Ky. Stat. 571.) Its ownership of all the stock of Louisville Trust Company and several other Kentucky state banks was expressly forbidden by Kentucky law. (Ky. Stat. 581, 609.) Except for a few days in October, 1929, when it first started business, all of its assets were in bank stocks and it never thereafter had any assets with which to pay an assessment

upon these bank stocks. It was never anything more than a corporate instrumentality of the shareholders in order that they might continue in the banking business, get all possible benefits therefrom and at the same time escape a statutory assessment in the event that one should be levied.

ROBERT S. MARX,
FRANK E. WOOD,
EDWARD M. BROWN,
HARRY KASFIR,
Attorneys for Petitioner.

Of Counsel,
NICHOLS, WOOD, MARX & GINTER.

APPENDIX

COPY OF STATUTES INVOLVED—ALL FROM UNITED STATES CODE, TITLE 12, BANKS & BANKING

§ 64. Individual liability of shareholders; transfer of shares.

The stockholders of every national banking association shall be held individually responsible for all contracts, debts, and engagements of such association, each to the amount of his stock therein, at the par value thereof in addition to the amount invested in such stock. The stockholders in any national banking association who shall have transferred their shares or registered the transfer thereof within sixty days next before the date of the failure of such association to meet its obligations, or with knowledge of such impending failure, shall be liable to the same extent as if they had made no such transfer, to the extent that the subsequent transferee fails to meet such liability; but this provision shall not be construed to affect in any way any recourse which such shareholders might otherwise have against those in whose names such shares are registered at the time of such failure. (Dec. 23, 1913, c. 6, § 23, 38 Stat. 273.)

§ 191. General grounds for appointment of receiver.

Whenever any national banking association shall be dissolved and its rights, privileges, and franchises declared forfeited, as prescribed in section 93, or whenever any creditor of any national banking association shall have obtained a judgment against it in any court of record, and made application, accompanied by a certificate from the clerk of the court stating that such judgment has been rendered and has remained unpaid for the space of thirty days, or whenever the comptroller shall become satisfied of the insolvency of a national banking association, he may, after due examination of its affairs, in either case, appoint a receiver who shall proceed to close up such association, and enforce the personal liability of the shareholders, as provided in section 192. (June 30, 1876, c. 156, § 1, 19 Stat. 63.)

§ 192. Default in payment of circulating notes.

On becoming satisfied, as specified in sections 131 and 132 of this title, that any association has refused to pay its circulating notes as therein mentioned, and is in default, the Comptroller of the Currency may forthwith appoint a receiver, and require of him such bond and security as he deems proper. Such receiver, under the direction of the comptroller, shall take possession of the books, records, and assets of every description of such association, collect all debts, dues, and claims belonging to it, and, upon the order of a court of record of competent jurisdiction, may sell or compound all bad or doubtful debts, and, on a like order, may sell all the real and personal property of such association, on such terms as the court shall direct; and may, if necessary to pay the debts of such association, enforce the individual liability of the stockholders. Such receiver shall pay over all money so made to the Treasurer of the United States, subject to the order of the comptroller, and also make report to the comptroller of all his acts and proceedings.

PROVIDED, That the comptroller may, if he deems proper, deposit any of the money so made in any regular Government depositary, or in any State or national bank either of the city or town in which the insolvent bank was located, or of a city or town as adjacent thereto as practicable; if such deposit is made he shall require the depositary to deposit United States bonds or other satisfactory securities with the Treasurer of the United States for the safe-keeping and prompt payment of the money so deposited:

PROVIDED, That no security in the form of deposit of United States bonds, or otherwise, shall be required in the case of such parts of the deposits as are insured under section 264 of this title. Such depositary shall pay upon such money interest at such rate as the comptroller may prescribe, not less, however, than 2 per centum per annum upon the average monthly amount of such deposits. (R. S. § 5234; May 15, 1916, c. 121, 39 Stat. 121; Aug. 23, 1935, c. 614, § 339, 49 Stat. 721.)